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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 702

THE NEBRASKA SEED COMPANY (TRANSFEROR IN REORGANIZATION WITH UNITED SEEDS INC.), AND UNITED SEEDS INC. (TRANSFEREE IN REORGANIZATION WITH THE NEBRASKA SEED COMPANY),

Petitioners,

vs.

THE UNITED STATES

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS AND BRIEF IN SUPPORT THEREOF.

O. L. DYKSTRA,
Counsel for Petitioners.

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Petitioners,

vs.

THE UNITED STATES

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS AND BRIEF IN SUPPORT THEREOF.

The Nebraska Seed Company (Transferor in Reorganization with United Seeds, Inc.) and United Seeds Inc. (Transferee in Reorganization with The Nebraska Seed Company), Petitioners herein, pray that a Writ of Certiorari issue to review the judgment and subsequent order of the United States Court of Claims entered respectively on December 1, 1953, and February 2, 1954, in the case numbered and entitled on its docket, No. 50274, The Nebraska Seed Company (Transferor in Reorganization with United Seeds

Inc.) and United Seeds Inc. (Transferee in Reorganization with The Nebraska Seed Company), Plaintiffs, versus United States of America, Defendant, which judgment dismissed petitioners' petition and which order overruled petitioners' motion to alter or amend judgment.

Opinion Below

The opinion of the United States Court of Claims (R. 26-25) is reported in 116 F. Supp. 740.

Summary Statement of the Matters Involved

This action was brought in the United States Court of Claims by the Petitioners for the refund of Federal income taxes in the amount of $16,930.16, together with interest allowable by law.

Petitioners, The Nebraska Seed Company and United Seeds Inc., are respectively transferee and transferor in a tax-free reorganization, under Section 112(b)(4) of the Internal Revenue Code, consummated as of August 1, 1947 (R. 8, and Exhibit 1, R. 10-19). Under the terms of the reorganization, The Nebraska Seed Company transferred all its assets (subject to all its liabilities) to United Seeds Inc. in exchange for certain shares of common stock of United States Inc. (Exhibit 1, R. 10-19). Subsequent to such transfer and exchange, The Nebraska Seed Company dissolved by exchanging its newly-acquired shares of United Seeds Inc. stock with its own shareholders for their stock in The Nebraska Seed Company.

Several years prior to the reorganization, in 1944, The Nebraska Seed Company had sold certain of its assets to the Yankton Realty Company and the Ralston Operating Company, with payment therefor to be made on an installment basis (Findings of Fact, R. 32). The Nebraska Seed Company elected to report the profit from such sales

on the installment basis as provided by Section 44(b) of the Internal Revenue Code and did report the profit from such sales consistently and correctly on the installment basis (Findings of Fact 5, R. 32). Included in the assets transferred to United Seeds Inc. by The Nebraska Seed Company were the balances on such installment contracts receivable (Findings of Fact 6, R. 32).

As of August 1, 1947, United Seeds Inc. also acquired in the same tax-free reorganization all of the assets and assumed all of the liabilities of certain other corporations including the Yankton Realty Company and the Ralston Operating Company (Findings of Fact 3, R. 32). Included in the liabilities assumed by United Seeds Inc. were the installment obligations of Yankton Realty Company and the Ralston Operating Company to The Nebraska Seed Company (Findings of Fact 6, R. 32). Consequently after the reorganization, United Seeds Inc. owned the installment contracts receivable as well as being obligated upon them.

On the final Federal income tax return for The Nebraska Seed Company, the remaining uncollected deferred profit on the installment sales was not reported (Findings of Fact 8, R. 33). On such final Federal income tax return for the short taxable period July 1, 1947, to July 31, 1947, The Nebraska Seed Company showed a net loss of $72,038.33, and using this as a basis filed timely claims for refund for the taxable years ending June 30, 1946, and June 30, 1947, claiming a tentative carry-back of net operating loss (Findings of Fact 11, R. 33). Based upon said claims for refund, the Collector of Internal Revenue paid back tentative tax refunds in the respective sums of $8,360.72 and $14,295.95 for the taxable years ending June 30, 1946, and June 30, 1947 (Findings of Fact 12, R. 33).

Within the period of limitation, the Commissioner of Internal Revenue examined the final Federal income tax re-

turn of The Nebraska Seed Company and determined that on such final return of that corporation the said remaining uncollected deferred profit from installment sales should be reported as income (Findings of Fact 13, R. 34). As a result of such examination by the Commissioner of Internal Revenue, a reassessment of a portion of the tax refunded was made against The Nebraska Seed Company. United Seeds Inc., as transferee and assignee in reorganization, paid such reassessment which is claimed to be refundable in this case (Findings of Fact 14, R. 34).

United Seeds Inc., as transferee, and The Nebraska Seed Company, as transferor, filed timely claims for refund with the Collector of Internal Revenue, seeking refunds of such taxes paid. The claims for refund were rejected (Findings of Fact 15, R. 34).

The United States Court of Claims rejected the respondent's contention that the remaining uncollected deferred profit from the installment sales should be reported as income on the final Federal income tax return of The Nebraska Seed Company (R. 30-31).

The Court, however, concluded that the tax should have been assessed against United Seeds Inc. as a separate taxpayer (R. 31). Despite the fact that United Seeds Inc. was only before the Court as transferee, the Court held that the burden of proving the absence of liability on the part of United Seeds Inc. as a separate taxpayer was on United Seeds Inc. as transferee (R. 31).

The respondent did not plead (R. 7-8) or prove (R. 8-25) a counterclaim against United Seeds Inc. as either a separate taxpayer or as transferee in reorganization.

Petitioners made timely motion to alter or amend judgment, or in alternative, to grant a rehearing or new trial (R. 35). It was petitioners' contention that the matter of whether United Seeds Inc., as a separate taxpayer, was

subject to a tax on the transaction before the Court was the proper basis of a counterclaim on behalf of the Defendant. In the alternative, the petitioners requested the Court to allow them to prove what the tax would have been if it had been properly assessed against United Seeds Inc. Both of these motions were overruled by the Court (R. 35).

Reasons Relied On for the Allowance of the Writ

I

IN THIS CASE THE UNITED STATES COURT OF CLAIMS HAS DEPARTED SO FAR FROM THE ACCEPTED AND USUAL COURSE OF JUDICIAL PROCEEDINGS AS TO CALL FOR AN EXERCISE OF THIS COURT'S POWER OF SUPERVISION.

Petitioners submit that the United States Court of Claims in its opinion departed so far and so erroneously from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

A

IN EFFECT, THE UNITED STATES COURT OF CLAIMS PLEADED AND PROVED A COUNTERCLAIM IN FAVOR OF THE RESPONDENT WITHOUT ALLOWING PETITIONERS AN OPPORTUNITY TO PLEAD, TO INTRODUCE PROOF, OR TO ARGUE IN DEFENSE OF SUCH COUNTERCLAIM.

This case involves an important question of Federal procedure which affects all tax cases litigated in the United States District Courts or the United States Court of Claims; namely, does the taxpayer, after proving his case, have to plead and prove the absence of all possible counterclaims in favor of the United States before he is allowed a refund of taxes?

In this case the Commissioner of Internal Revenue claimed that The Nebraska Seed Company owed a tax because it transferred installment contracts receivable to

United Seeds Inc. in a tax-free reorganization (Findings of Fact 13, R. 34). Since at the time of the assessment of the tax The Nebraska Seed Company had already been dissolved, United Seeds Inc. paid the tax as transferee in reorganization (Findings of Fact, R. 34).

The petitioners proved to the United States Court of Claims that The Nebraska Seed Company was not liable for the tax assessed (R. 30-31). Although no counterclaim was pleaded or proved (R. 7-8, R. 8-25), the Court held that the petitioners could not recover the tax because they had failed to prove what the tax would have been if it had been properly assessed against United Seeds Inc. in its proper taxable period, which taxable period was not before the Court.

It is respectfully submitted that such holding by the United States Court of Claims is in direct conflict with its own Rule 17 relating to counterclaims as well as its decisions in *Enright* v. *The United States,* 73 Ct. Cls. 416, 54 F. 2d 182, Cert. Denied 286 U. S. 543 (1932) and *Mohawk Condensed Milk Company* v. *The United States,* 70 Ct. Cls. 671 (1930). Such holding is also in conflict with the decision of the United States Court of Appeals for the Fifth Circuit in *Co-Efficient Foundation* v. *Woods,* 171 F. 2d 691 (CCA-5, 1949).

Furthermore, Federal Rule 13 governing counterclaims in the United States District Courts is practically identical to Rule 17 of the United States Court of Claims. Therefore, to allow the decision of the United States Court of Claims to stand in this case would constitute authority for the proposition that every taxpayer seeking a refund of Federal taxes in all forums available to him must plead and prove himself free of any possible counterclaim by the United States in addition to pleading and proving his own case.

It is respectfully submitted that such a burden would in effect preclude the taxpayer from using either the United States District Court or the United States Court of Claims as a forum to litigate his tax disputes with the Federal Government.

B

THE UNITED STATES COURT OF CLAIMS ALLOWED THE UNITED STATES TO USE A CLAIM AGAINST A TAXPAYER NOT BEFORE THE COURT AS A BASIS FOR A COUNTERCLAIM AGAINST THE PETITIONERS.

United Seeds Inc. was a party in this case only as transferee in reorganization (Findings of Fact 14, R. 34). This resulted because it had paid the tax assessed against its transferor, The Nebraska Seed Company (Findings of Fact 14, R. 34). It was not before the Court in the capacity of a separate or individual taxpayer.

The United States Court of Claims held that The Nebraska Seed Company was not liable for the tax assessed against it (R. 30-31). It is submitted that if The Nebraska Seed Company had no liability on the tax, neither did United Seeds Inc. in its capacity as transferee of The Nebraska Seed Company since such liability is but secondary. If this be so, it means that the United States Court of Claims denied recovery to the petitioners because it allowed a counterclaim of the United States against a taxpayer not before the Court (United Seeds Inc. as a separate and individual taxpayer) to be off-set against the recovery due the petitioners.

In thus failing to distinguish between United Seeds Inc. as a transferee of The Nebraska Seed Company and United Seeds Inc. as a separate and individual taxpayer, the United States Court of Claims, it is submitted, so far departed from the usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

Jurisdiction

The judgment of the United States Court of Claims was entered December 1, 1953 (R. 26). Plaintiff's motion to alter or amend judgment or, in alternative, to grant a rehearing or new trial was overruled by the Court on February 2, 1954 (R. 35). The jurisdiction of this Court is invoked under Title 28, United States Code, Sections 1255(1), 1651(a) and 2101(c).

Statutes and Regulations Involved

Sections 44(d) and 112(b)(4) of the Internal Revenue Code, as amended, together with pertinent provisions of the regulations issued thereunder, are set forth in Appendix A, infra, pp. 20 and 21.

Questions Presented

1. Whether the United States Court of Claims erred in placing the burden on the plaintiffs of pleading and proving the absence of a possible counter-claim in favor of the defendant?

2. Whether the United States Court of Claims erred in failing to distinguish between a taxpayer, as a transferee, and a taxpayer in its individual capacity?

3. Whether the United States Court of Claims erred in failing to recognize that there was no taxable period of United Seeds Inc. before it for review?

4. Whether the United States Court of Claims erred in failing to give judgment to the petitioners after finding that petitioner, The Nebraska Seed Company, was not liable for the tax assessed against it by the respondent?

Conclusion

For the foregoing reasons, it is respectfully submitted this petition for writ of certiorari should be granted.

O. L. Dykstra,
Attorney for Petitioners.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

Summary of Argument

I

The United States Court of Claims erred in holding that petitioners had to prove what the tax would have been if properly assessed against United Seeds Inc. as a separate taxpayer in its proper taxable period because such issue properly constituted the basis of a counterclaim by the respondent under Rule 17 of the United States Court of Claims which respondent had the burden to plead and prove.

II

The United States Court of Claims erred in allowing a claim against a taxpayer not before the Court to be used as a basis for a counterclaim against the petitioners.

ARGUMENT

I

THE UNITED STATES COURT OF CLAIMS ERRED IN HOLDING THAT PETITIONERS HAD TO PROVE WHAT THE TAX WOULD HAVE BEEN IF PROPERLY ASSESSED AGAINST UNITED SEEDS INC. AS A SEPARATE TAXPAYER IN ITS PROPER TAXABLE PERIOD BECAUSE SUCH ISSUE PROPERLY CONSTITUTED THE BASIS OF A COUNTERCLAIM BY THE RESPONDENT UNDER RULE 17 OF THE UNITED STATES COURT OF CLAIMS WHICH RESPONDENT HAD THE BURDEN TO PLEAD AND PROVE.

The tax involved in this case was paid by United Seeds Inc. as transferee and assignee in reorganization of The Nebraska Seed Company (Findings of Fact 14, R. 34). The United States Court of Claims concluded that respondent's assessment against The Nebraska Seed Company was wrong

and that no tax was due from it on the transaction before the Court; (R. 30-31). Therefore, it is submitted that there can be no liability on United Seeds Inc., as transferee in reorganization.

The situation here at hand is analogous to the subject of transferee liability under Section 311 of the Internal Revenue Code. It is fundamental in tax law that the liability of a transferee in such cases is not primary but secondary. *Oswego Falls Corp.*, 26 BTA 60, aff'd 71 F. 2d 673 (CCA 2d, 1934); *Comm.* v. *Estate of Hunt Henderson*, 147 F. 2d 619 (CCA-5, 1945). Therefore, by analogy, if the transferor (The Nebraska Seed Company) owed no tax on the transaction before the United States Court of Claims, as such Court held (R. 30-31), then neither did the transferee (United Seeds Inc.) as such.

In Volume 9 of Mertens, *Law of Federal Income Taxation*, the author makes the following statements concerning the subject of transferee liability under Section 311 of the Internal Revenue Code:

* * * * * * *

"#53.10 Elements of Transferee Liability.
* * * the following elements of liability are generally a condition to transferee liability:

* * * * * * *

"(2) The transferor must have been liable;

* * * * * * *

"#53.26 Liability of the Transferor is Essential to Transferee Liability. *Transferee liability is based fundamentally upon the existence of a tax liability on the part of the transferor.* If the alleged transferor had no assets and was not engaged in business during the period in question, it can have no income, and the transferee cannot be liable as such. * * * If the transferee can prove that the transferor had no tax liability, it follows that a transfer of assets to the trans-

feree was not fraudulent insofar as the Government is concerned.

"#53.27 * * * A necessary corollary to this rule of *res judicata* is that the Commissioner in a transferee proceeding cannot attack the amount of deficiency which the Board has already determined in a proceeding against the transferor. *Thus, if the Board has determined in the case of the transferor that there was no tax liability, none can be asserted against the transferees.* * * *." (Emphasis supplied)

It is respectfully submitted that, inasmuch as the United States Court of Claims held that the transferor in reorganization, The Nebraska Seed Company, owed no tax on the transaction before the Court, it must necessarily follow that United Seeds, Inc., *as transferee in reorganization*, owed no tax on the transaction. Since the tax was assessed against The Nebraska Seed Company as transferor and paid by United Seeds Inc. as transferee (Findings of Fact 14, R. 34), and since The Nebraska Seed Company proved it had no liability on the tax as transferor in reorganization, United Seeds Inc. could have no liability as transferee in reorganization and the right to the refund of tax claimed was established.

Despite the foregoing, the United States Court of Claims ignored the concept of separate and distinct taxable entities and proceeded to a finding that United Seeds Inc. *not* because of its status as a transferee in reorganization, but in its individual and separate capacity, had realized income and then concluded as follows (R. 31):

"* * * Since United Seeds Inc. is the company now entitled to receive any refund of these taxes, and since it was this company in whose hands the balance due on the installment sales was satisfied, and who, if anyone, owes the tax on the profit, this company should not be permitted to recover this refund.

"It may be that if the tax were now assessed against

United Seeds Inc., it might not amount to exactly the same sum as that assessed against The Nebraska Seed Company. If there was a difference, the burden of showing this was on plaintiffs."

The Court therefore concluded, without the benefit of pleading or proof, that United Seeds Inc. as a separate and individual taxpayer was liable for a tax on the transaction before it. The Court admitted that it had no way of knowing what the tax should have been if properly assessed against United Seeds Inc. as a separate taxpayer in its proper taxable year. The Court, however, was unconcerned about this matter because "the burden of showing this was on Plaintiffs."

But why was this burden on the petitioners in view of Rule 17 of the United States Court of Claims? This rule states in part:

"Rule 17. COUNTERCLAIMS

"(a) Compulsory Counterclaims. *The answer shall state as a counterclaim any claim which* at the time of serving the answer *the defendant has against any plaintiff*, if it arises out of the transaction or occurrence that is the subject matter of the petition and does not require for its adjudication the presence of third parties to whom the Court cannot acquire jurisdiction. • • •.

"(b) Permissive Counterclaims. *The answer may state as a counterclaim any claim against plaintiff* not arising out of the transaction or occurrence that is the subject matter of the petition." (Emphasis Supplied)

Further, the rules of the United States Court of Claims provide relief to a defendant who overlooks a counterclaim in its pleadings by providing in subsection (e) of Rule 17:

"When defendant fails to set up a counterclaim through oversight, inadvertence, or excusable neglect, or when justice requires, it may by leave of Court set up the counterclaim by amendment."

The respondent here did not choose to explore the use of this rule either, even though the rule was set up for its benefit for possible overlooked counterclaims.

With respect to the nature of counterclaims, whether the claim which the Court held the respondent to have against petitioners was a compulsory or permissive counterclaim is not germane in this proceeding. It is germane, however, to determine if such claim was a counterclaim. It seems clear to the petitioners the words "any claim" in Rule 17 must encompass what the Court concluded that the respondent had against United Seeds Inc. as a separate taxpayer.

Although the Petitioners have not been able to find authority which interprets Rule 17 of the United States Court of Claims, they believe that the learned comments of Professor James Wm. Moore and of Barron and Holtzoff on the practically identical Federal Rule 13 are equally applicable to Rule 17 of the United States Court of Claims. Federal Rule 13(a) and (b) states in part:

> "13(a) Compulsory Counterclaims. A pleading shall state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party's claim and does not require for its adjudication the presence of third parties of whom the Court cannot acquire jurisdiction, * * *.
>
> "13(b) Permissive Counterclaim. A pleading may state as a counterclaim any claim against an opposing party not arising out of the transaction or occurrence that is the subject matter of the opposing party's claim."

Professor Moore, in Volume 3 of *Moore's Federal Practice*, states in regard to Federal Rule 13(a) and (b):

> "§ 13.02 Analysis and scope of Rule 13:
>
> Rule 13 applies to two types of claims: counterclaims and cross-claims. *Under this rule a counterclaim is*

any claim, including set-off and recoupment, which one party has against an opposing party, whether legal or equitable, or both. Thus, any claim which a defendant has against the plaintiff is a counterclaim; * * *"

* * * * * * *

"§ 13.18 General Scope of Rule 13b(b):

Subdivision (b) applies to any claim that one party may have against an opposing party, not of a compulsory character. Its purpose is to give the same freedom to the pleading of independent claims by a defendant against a plaintiff (or plaintiffs) as the plaintiff (or plaintiffs) has in pleading claims against a defendant or defendants * * *." (Emphasis Supplied)

Barron and Holtzoff, *Federal Practice and Procedure*, in § 393, at page 790, say with respect to Federal Rule 13:

"The rule is comprehensive and elastic. The term 'counterclaim' has been often judicially defined. Under the rules a 'counterclaim' embraces 'any claim which at the time of serving the pleading the pleader has against any opposing party', and may include a claim for recoupment, restitution or set-off. The counterclaim, set-off or recoupment may be legal or equitable and is available to the United States as well as other litigants. * * *"

It is submitted that Rule 17 of the United States Court of Claims is as equally broad and comprehensive as Federal Rule 13. Both rules include all claims and off-sets which the defendant has against the plaintiff. It must necessarily include what the Court held to be respondent's right against petitioners because of the Court's conclusion that United Seeds Inc. as a separate taxpayer should have paid the tax.

It seems clear that once the United States Court of Claims had decided that The Nebraska Seed Company had no liability, and impliedly therefore that United Seeds Inc. had no liability as transferee in reorganization, then to deny the

petitioners relief must be on a basis of allowing a counterclaim by the respondent. But the respondent did not plead a counterclaim; the respondent did not prove a counterclaim; the respondent did not show the Court the legal basis upon which a counterclaim could rest. More important, the petitioners had no opportunity to resist such action because they were first advised of such action upon rendition of the opinion of the Court and their subsequent motion to allow themselves to introduce proof on the matter was overruled by the Court.

That the defendant has the burden of proving a counterclaim seems well established in the decisions of the United States Court of Claims. In *Enright* v. *The United States*, 73 Ct. Cls. 416, 54 F. 2d 182, Cert. Denied 286 U. S. 543 (1932), one of the issues involved who had the burden of proving a counterclaim. In holding for the plaintiff on this issue, the Court said at page 431:

> "The remaining contention on behalf of the Plaintiffs is that in the instant case the burden of proof is on the defendant to show the amount of just compensation, and if just compensation is not to be ascertained in the manner for which plaintiffs contend the proof fails to show the amount thereof. Counsel for defendant has assumed that the burden was on the plaintiffs to establish the amount of just compensation. We do not think this is correct. * * * *The defendant is suing upon a counterclaim.* * * * *The burden of proof is upon the defendant to show that the plaintiffs have no right to retain this fund and that in fact it belongs to defendant.*" (Emphasis supplied.)

And in *Mohawk Condensed Milk Company* v. *The United States*, 70 Ct. Cls. 671 (1930), the United States Court of Claims said of the burden of proof on a counterclaim at page 678:

> "Inasmuch as we have no competent evidence to establish the correctness of the figures for which the defend-

ant contends, we cannot allow any portion of the counterclaim * * *. *We need not discuss this feature in view of the lack of competent proof by the defendant to support its counterclaim on its theory.*" (Emphasis supplied.)

That the defendant should have the burden of proving his counterclaim seems fundamental in the law of procedure and cannot be validly contested. The only case the petitioners have been able to find which deals with this aspect of the Federal Rules is *Co-Efficient Foundation* v. *Woods*, 171 F. 2d 691 (CCA-5, 1949). In this case the Fifth Circuit said at page 694:

> "Counterclaim, set-off, recoupment, and the like are in the nature of affirmative remedies which the defendant has the burden of pleading and proving, and the trial court will not be put in error for appellants' own omissions, or for failing to do that which they did not timely request. * * *"

It is respectfully submitted that the action of the United States Court of Claims in shifting the burden of the counterclaim from the respondent to the petitioners was an erroneous departure from the accepted and usual course of judicial proceedings and requires an exercise of this Court's power of supervision. It is further submitted that the action of the United States Court of Claims has dangerous implications.

A taxpayer may litigate his tax disputes with the Federal Government in three forums: the Tax Court of the United States, the United States District Court, and the United States Court of Claims. He may obtain a jury trial on the factual issues only in the United States District Court.

The petitioners believe that the decision of the United States Court of Claims must be interpreted to stand for the proposition that the taxpayer is imposed with the additional

burden of proving himself free of all possible counterclaims in favor of the United States. Because of the practical identity of Rule 17 of the United States Court of Claims with Federal Rule 13, it is believed that if the decision below is allowed to stand, authority will be established which also effects the taxpayer's burden in litigating his controversies in the United States District Courts.

It is further believed that such an additional burden on the taxpayer would be so onerous as to preclude his effective use of either the United States District Court or the United States Court of Claims. If this be so, the taxpayer would be precluded as a practical matter from the only forum—the United States District Court—where he might have the factual issues tried by a jury.

II

THE UNITED STATES COURT OF CLAIMS ERRED IN ALLOWING A CLAIM AGAINST A TAXPAYER NOT BEFORE THE COURT TO BE USED AS A BASIS FOR A COUNTERCLAIM AGAINST THE PETITIONERS.

The United States Court of Claims held that United Seeds Inc. as a separate taxpayer was liable for the tax on the transaction before it for review by concluding: "The deferred profit, therefore, was realized not by Nebraska Seed Company, but by United Seeds, Inc." (R. 31). Consequently, the Court refused to allow United Seeds Inc. as transferee in reorganization with The Nebraska Seed Company to recover the tax refund because the Court felt that United Seeds Inc. as a separate taxpayer should have paid the tax.

United Seeds Inc. as a separate taxpayer was not before the Court. The Court below therefore refused to allow petitioners' recovery of the tax refund because of an obligation of a taxpayer not before the court which, petitioners submit, the Court below allowed to be used as a basis of an unpleaded

and unproved counterclaim against the petitioners' established right to a refund.

Furthermore, the Court below disregarded the concept of individual taxable periods. The taxable years before the Court below are the years ended June 30, 1946, and June 30, 1947, and the short period from July 1, 1947, to July 31, 1947. (Paragraphs 5 to 8, inclusive, of petition, admitted in answer, R. 7). These years cover the operations of the petitioner, The Nebraska Seed Company, and do not involve the operations of the petitioner, United Seeds Inc., as a separate taxpayer. If a tax is due from United Seeds Inc. as a separate taxpayer, as the Court concluded, it must be on the basis that United Seeds Inc. as a separate taxpayer was, as the Court said, the "company in whose hands the balance due on the installment sales was satisfied" (R. 31). Such balance due on the installment sales was satisfied in the hands in United Seeds Inc. when, after the reorganization, the United Seeds Inc. owned the installment contracts receivable as well as being obligated upon them (R. 30). If a tax is due from United Seeds Inc. because of the satisfaction of the installment obligations in its hands, it is due from that company as a separate taxpayer for the taxable period in which satisfaction took place. This taxable period would be the taxable period of United Seeds Inc. within which period the reorganization took place, and which taxable period was not before the Court.

Conclusion

For all the reasons stated, writ of certiorari should be granted in this cause, and this Court should review the decision of the United States Court of Claims and finally reverse it.

Respectfully submitted,

O. L. Dykstra,
Counsel for Petitioners.

APPENDIX "A"

STATUTES AND REGULATIONS

Section 44(d) of the Internal Revenue Code, as amended:

"SEC. 44. INSTALLMENT BASIS.

* * * * *

(d) Gain or Loss Upon Disposition of Installment Obligation. If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. Any gain or loss so resulting shall be considered as resulting from the sale or exchange of the property in respect of which the installment obligation was received. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full. This subsection shall not apply to the transmission at death of installment obligations if there is filed with the Commissioner, at such time as he may by regulation prescribe, a bond in such amount and with such sureties as he may deem necessary, conditioned upon the return as income, by the person receiving any payment on such obligations, of the same proportion of such payment as would be returnable as income by the decedent if he had lived and had received such payment. If an installment obligation is distributed by one corporation to another corporation in the course of a liquidation, and under section 112(b)(6) no gain or loss with respect to the receipt of such obligation is recognized in the case of the recipient corporation, then no gain or loss with respect to the distri-

bution of such obligation shall be recognized in the case of the distributing corporation."

Section 112(b)(4) of the Internal Revenue Code, as amended:

"SEC. 112. RECOGNITION OF GAIN OR LOSS.

"(b) Exchanges Solely in Kind.—

(4) Same—gain of corporation. No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization."

* * * * *

Treasury Regulations 111, pertaining to Section 44(d) of the Internal Revenue Code:

"Sec. 29.44-5 (As Amended by T. D. 5334, Feb. 28, 1944). Gain or loss upon disposition of installment obligations.—The entire amount of gain or loss resulting from the disposition or satisfaction of installment obligations, computed in accordance with section 44(d), is recognized under the Internal Revenue Code unless the disposition is within one of the exceptions made by the Code. Such an exception is provided in Section 44(d) with respect to distributions under Section 112 (b)(6), and in Section 112(b)(4) and (5) with respect to exchanges."

* * * * *

Treasury Regulations 111, pertaining to Section 112(b)(4) of the Internal Revenue Code:

"Sec. 29.112(a)-1 (As Amended by T. D. 5356, April 19, 1944, and T. D. 5402, Sept. 5, 1944). Sales or exchanges—The extent to which the amount of gain or loss, determined under section 111, from the sale or exchange of property is to be recognized is governed by the provisions of section 112. The general rule is

that the entire amount of such gain or loss is to be recognized.

"Exceptions to the general rule are made by sections 112(b)(1) to (5), inclusive, section 112(b)(10) and section 112(1) in the case of certain specifically described exchanges of property in which at the time of the exchange particular differences exist between the property parted with and the property acquired, but such differences are more formal than substantial. As to these, the Internal Revenue Code provides that such differences shall not be deemed controlling, and that gain or loss shall not be recognized at the time of the exchange. The underlying assumption of these exceptions is that the new property is substantially a continuation of the old investment still unliquidated; and, in the case of reorganizations, that the new enterprise, the new corporate structure, and the new property are substantially continuations of the old still unliquidated."

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301892—54——1

In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 702

THE NEBRASKA SEED COMPANY (TRANSFEROR IN REORGANIZATION WITH UNITED SEEDS, INC.), AND UNITED SEEDS, INC., (TRANSFEREE IN REORGANIZATION WITH THE NEBRASKA SEED COMPANY), PETITIONERS

v.

THE UNITED STATES

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the United States Court of Claims (R. 26–35) is reported in 116 F. Supp. 740.

JURISDICTION

The opinion and judgment of the Court of Claims were entered December 1, 1953. (R. 26.) Motions to alter or amend the judgment or to grant a rehearing or new trial were filed on

December 28, 1953, and were denied on February 2, 1954. (R. 35.) The petition for a writ of certiorari was filed on April 20, 1954. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1255 (1).

QUESTION PRESENTED

The taxpayer acquired all the assets (which included unpaid balances owing on installment sales) from another corporation in a nontaxable exchange. Simultaneously, also in a nontaxable exchange, the taxpayer acquired the assets and assumed the obligations of two other corporations which were the purchasers under the installment contracts. The liabilities assumed by the taxpayer included the unpaid balances on the installment contracts and these liabilities were thus extinguished. Neither the taxpayer nor its predecessor obligee reported any income on the transfer and extinction of the installment obligations. The Court of Claims decided that no gain was recognizable to the transferor corporation on the transfer of the installment obligations but that the deferred profit became taxable to the taxpayer when the obligations were extinguished.

The question is whether the Court of Claims was correct in deciding that, since the taxpayer was liable for but had failed to pay the tax on these profits, it was not entitled to a refund of the tax on the same profits which it had paid as transferee of the transferor corporation.

STATUTES INVOLVED

The applicable portions of the pertinent statutes are set forth in the Appendix, *infra*, pp. 12–14.

STATEMENT

The findings of fact of the Court of Claims may be summarized as follows:

The taxpayer, Nebraska Seed Company, hereinafter referred to as "Nebraska", was a corporation organized under the laws of the State of Nebraska. The taxpayer United Seeds, Inc., hereinafter referred to as "United", is a corporation organized under the laws of the State of Delaware, but with its principal place of business in Ralston, Nebraska. (R. 31–32.)

As of August 1, 1947, United acquired all of the assets and assumed all of the liabilities of Nebraska, pursuant to a plan of reorganization dated July 25, 1947, in exchange for shares of United capital stock. Such reorganization was tax free under the provisions of Section 112 (b) (4) of the Internal Revenue Code. (R. 32.)

As of August 1, 1947, United also acquired under the plan of reorganization all of the assets and assumed all of the liabilities of certain other corporations including the Yankton Realty Company and the Ralston Operating Company. The assets of all these companies were taken in exchange for shares of capital stock of United. The reorganization of these companies was also

a so-called tax free reorganization under Section 112 (b) (4) of the Internal Revenue Code. (R. 32.)

Several years prior to the reorganization, in 1944, Nebraska had sold certain of its assets to the Yankton Realty Company and the Ralston Operating Company, with payment therefor to be made on an installment basis. Nebraska elected to report the profit from such sales on the installment basis as provided by Section 44 (b) of the Internal Revenue Code and did report the profit from such sales consistently and correctly on the installment basis. (R. 32.)

Included in the obligations assumed by United in the plan of reorganization were the installment obligations of Yankton Realty Company and the Ralston Operating Company to Nebraska, and included in the assets received by United were the receivables from these companies which were held by Nebraska. By July 31, 1947, Nebraska had deferred profit on the installment sale which was not reported for federal income tax purposes in the sum of $45,338.39. On the final federal income tax return for Nebraska, the deferred profit was not reported as income. (R. 32–33.)

Under the plan of reorganization of United after the merger of the five corporations, including Nebraska, the Yankton Realty Company and the Ralston Operating Company, all of the assets of Nebraska were transferred to United in ex-

change for shares of stock of the latter corporation on the basis of two shares of $1 par value stock for each $3 value of Nebraska's net worth. In computing the value of the net worth of Nebraska for this purpose, it was permitted to include in its surplus the unrealized profit from the installment obligation due from the Yankton Realty Company and the Ralston Operating Company as the result of the sales of property by Nebraska to those companies in 1944. After this exchange, the stock received from United by Nebraska was distributed to the stockholders of Nebraska, which was then dissolved. (R. 33.)

For the taxable years ending June 30, 1946, and June 30, 1947, Nebraska paid income taxes to the Collector of Internal Revenue at Omaha, Nebraska, in the amounts of $8,360.72 and $17,322.58. For the short taxable period July 1, 1947, to July 31, 1947, Nebraska filed a final federal income tax return showing a net loss of $72,038.33, and using this as a basis filed timely claims for refund for the taxable years ending June 30, 1946, and June 30, 1947, claiming a tentative carry-back of net operating loss of the years ending June 30, 1946, and 1947, in accordance with the provisions of Section 3780 of the Internal Revenue Code. The Collector of Internal Revenue paid tentative tax refunds in the respective sums of $8,360.72 and $14,295.95 for the

taxable years ending June 30, 1946, and June 30, 1947. (R. 33-34.)

Within the period of limitation, the Commissioner of Internal Revenue examined the final federal income tax return of Nebraska and determined that on the final return of that corporation the remaining uncollected deferred profit from installment sales should be reported as income. As a result of the examination a reassessment of a portion of the tentative refunds made under Section 3780 of the Internal Revenue Code resulted and United, as transferee and assignee in reorganization, on or about July 12, 1950, paid the respective sums of $1,416.53 and $14,039.14 in federal income taxes for the taxable years ending June 30, 1946, and June 30, 1947, together with interest in the amounts of $86.70 and $1,336.02 for the respective taxable years. (R. 34.)

On or about October 24, 1950, the taxpayers filed timely claims for refund seeking refunds in the respective sums of $1,416.53 and $14,090.91 for the taxable years ending June 30, 1946, and June 30, 1947, together with interest and/or other amounts properly refundable, using as the basis of their claims the net operating loss carry-backs from the short taxable year from July 1, 1947, to July 31, 1947, to the taxable years ending June 30, 1946, and June 30, 1947. The claims for refund were rejected on July 27, 1951. (R. 34.)

On the basis of the foregoing facts, the Court of Claims concluded that the taxpayers were not entitled to recover and dismissed their petition. Following the judgment of the court, the taxpayers, on December 28, 1953, filed motions to alter or amend judgment or, in the alternative, to grant a rehearing or new trial. The court overruled these motions on February 2, 1954. (R. 35.)

ARGUMENT

1. The decision of the Court of Claims is correct. If, as the court below held, Nebraska did not become taxable with the deferred profits on the installment contracts when they were transferred to United, it is clear that United did become taxable with those profits when, simultaneously, the obligations were extinguished as a result of United's assumption of the obligations of the two corporations which were originally indebted to Nebraska. United, which had successfully urged on the Court of Claims the proposition that Nebraska had incurred no tax liability, does not assert that the profits did not become taxable to it when it became both obligor and obligee and the installment obligations were thereby extinguished. Any such assertion, had it been made, would have been fruitless in view of the provisions contained in the first sentence of Code Section 44 (d) (Appendix, *infra*, pp. 12–13) and its legislative history (H. Rep. No. 2, 70th Cong., 1st Sess., p. 16

(1939–1 Cum. Bull. (Part 2) 384, 394–395)). Nor does United assert that, contrary to the finding of the Court of Claims (R. 31), it had reported this income as its own and had paid the tax.

Under these circumstances, in this refund suit, United was clearly not entitled to a judgment against the United States since it was liable for the tax on the very item of income which gave rise to the refund claim. *Stone* v. *White*, 301 U. S. 532, 535. It would be idle to permit United as transferee to obtain a refund and then adjudge it primarily liable on the same tax. Any refund of tax to which United might be entitled was offset by a tax in the same or substantially the same amount. The ultimate question involved in the claim for refund is whether the taxpayer has overpaid its tax. There has been no showing that United or its predecessor did overpay the tax. In the absence of such a showing, the Government has the right to retain payments already received. *Stearns Co.* v. *United States*, 291 U. S. 54, 62–63; *Lewis* v. *Reynolds*, 284 U. S. 281; *Stone* v. *White*, 301 U. S. 532.

2. There is no merit to the taxpayer's contention that the Court of Claims failed to follow its own Rule 17 with respect to counterclaims. (Br. 14–16.) In general, a counterclaim involves a counter demand containing elements necessary to constitute an independent action for affirmative relief, and not mere defensive matter in denial of

the original claim. *United States* v. *Shaw*, 309 U. S. 495, 503. Rule 17 of the Court of Claims, in accordance with its statutory authority (28 U. S. C., Section 1503), broadens the scope of counterclaims to include claims against a plaintiff not arising out of the transaction or occurrence that is the subject matter of the petition, but neither the statute nor the Rules of the Court of Claims narrows the usual concept of a counterclaim to include a defense to recovery not embracing an independent action for affirmative relief.

Here no counterclaim was pleaded nor can one be inferred to have been demanded. There was only one tax involved, pertaining to the same unreported income, and since Nebraska was dissolved before the action commenced, United was actually the only taxpayer before the court below. Whether the liability for the tax was Nebraska's or United's has become moot in view of the merger leaving United alone as the claimant of the refund, and as the one who owes the tax on the unreported deferred profit. No formal plea of counterclaim was required to prevent the taxpayer from obtaining a refund to which it was not entitled, for at most the matter was in the nature of a setoff. As this Court said in *Stone* v. *White*, 301 U. S. 532, 539: "Here the defense is not a counter demand * * *." See also *Wisconsin Central R'd* v. *United States*, 164 U. S. 190, 212; *Vulcanite Cement Co.* v. *United States*, 74 C. Cls.

692, 717; *United States* v. *Drescher,* 179 F. 2d 863 (C. A. 2d), certiorari denied, 340 U. S. 821.

There is no merit to the taxpayers' contention that United was not before the court below except in a transferee capacity. While United had paid the tax as Nebraska's transferee, United was seeking the refund as its own and, quite plainly, it was not entitled to be enriched in this manner when it was liable for and had not paid the tax on the disputed item of income. Neither can any significance be found in taxpayers' point that separate taxable periods are involved. (Br. 19.) In *United States* v. *Drescher, supra,* where the taxpayer successfully argued that an item of income was not realized in one year, the court, nevertheless, refused to allow the refund in the absence of a showing that the tax had been paid for the other year when it was realized as income. Here, whether recognized to Nebraska or United, the item became income on August 1, 1947.

3. There is no conflict of decisions, and none is alleged in the petition. The taxpayers' attempt to portray this as a case of importance requiring review by this Court ultimately rests on the assumption that the decision below stands for the proposition that a taxpayer has the (Br. 18) "burden of proving himself free of all possible counterclaims in favor of the United States." As we have shown, however, no question of counterclaim is involved and the decision below cannot be interpreted in such a manner.

CONCLUSION

The decision of the court below is correct. This case presents no conflict of decisions, and no question of public interest or importance. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JUNE 1954.

APPENDIX

Internal Revenue Code:

SEC. 44. INSTALLMENT BASIS.

* * * * *

(d) *Gain or Loss upon Disposition of Installment Obligations.*—If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. Any gain or loss so resulting shall be considered as resulting from the sale or exchange of the property in respect of which the installment obligation was received. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full. This subsection shall not apply to the transmission at death of installment obligations if there is filed with the Commissioner, at such time as he may by regulation prescribe, a bond in such amount and with such sureties as he may deem necessary, conditioned upon the return as income, by the person receiving any payment on such obligations, of the same proportion of such payment as would be re-

turnable as income by the decedent if he had lived and had received such payment. If an installment obligation is distributed by one corporation to another corporation in the course of a liquidation, and under section 112 (b) (6) no gain or loss with respect to the receipt of such obligation is recognized in the case of the recipient corporation, then no gain or loss with respect to the distribution of such obligation shall be recognized in the case of the distributing corporation.

(26 U. S. C. 1946 ed., Sec. 44.)

SEC. 112. RECOGNITION OF GAIN OR LOSS.

* * * * *

(b) *Exchanges Solely in Kind.*—

* * * * *

(4) *Same.—Gain of corporation.*—No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization.

* * * * *

(6) *Property received by corporation on complete liquidation of another.*—No gain or loss shall be recognized upon the receipt by a corporation of property distributed in complete liquidation of another corporation. For the purposes of this paragraph a distribution shall be considered to be in complete liquidation only if——

(A) the corporation receiving such property was, on the date of the adoption of the plan of liquidation, and has continued to be at all times until the receipt of the

property, the owner of stock (in such other corporation) possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and the owner of at least 80 per centum of the total number of shares of all other classes of stock (except non-voting stock which is limited and preferred as to dividends), and was at no time on or after the date of the adoption of the plan of liquidation and until the receipt of the property the owner of a greater percentage of any class of stock than the percentage of such class owned at the time of the receipt of the property; and

* * * * *

(26 U. S. C. 1946 ed., Sec. 112.)

U. S. GOVERNMENT PRINTING OFFICE: 1946